Supreme Court of the United States

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NO.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1964

TENNESSEE PRODUCTS & CHEMICAL CORPORATION, PETITIONER

vs.

UNITED STATES OF AMERICA

Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

Tennessee Products & Chemical Corporation petitions for a writ of certiorari to review the judgment of the Court of Appeals for the Sixth Circuit in this case (No. 14,522 below).

OPINION BELOW

The findings of fact and conclusions of law of the District Court (R. 22a-29a)[1] together with the District Court's memorandum, are reported at 199 F. Supp. 885. The per curiam opinion of the Court of Appeals (App., *infra*, pp. 7-8) is reported at 297 F. 2d 529.

[1] Record references are to the appendix to appellant's brief in the Court below.

JURISDICTION

The judgment of the Court of Appeals was entered January 4, 1962. (App., *infra*, p. 9). Petition for rehearing was filed and denied February 13, 1962. (App., *infra*, p. 9). The jurisdiction of this Court is invoked under 28 U. S. C. 1254(1).

QUESTION PRESENTED

In determining whether indebtedness existed in 1942, susceptible of being charged off as partially worthless by a federal income taxpayer, whether a state court judgment entered in 1942, allowing the taxpayer's claim on the indebtedness in a proceeding for the distribution of an insolvent estate, was entitled to full faith and credit in a federal court, or did the court properly disregard the state court judgment on the ground that an available defense had not actually been considered by the state court?

STATUTE INVOLVED

Title 28, sec. 1738, U. S. Code, reads in relevant part as follows:

"§ 1738. State and Territorial statutes and judicial proceedings; full faith and credit

* * * * *

"The records and judicial proceedings of any court of any such State, Territory or Possession, or copies thereof, shall be proved or admitted in other courts within the United States and its Territories and Possessions by the attestation of the clerk and seal of the court annexed, if a seal exists, together with a certificate of a judge of the court that the said attestation is in proper form.

"Such Acts, records and judicial proceedings or copies thereof, so authenticated, shall have the same full faith and credit in every court within the United States and its Territories and Possessions as they have by law or usage in the courts of such State, Territory or Possession from which they are taken." (June 25, 1948, ch. 646, 62 Stat. 947.)

STATEMENT

The undisputed facts may be summarized as follows:

In 1931 the Executive Committee of the petitioner corporation reduced the salary of W. J. Cummins, an officer, from $36,000 a year to $12,000 a year, but permitted him to overdraw his personal account with the corporation, with the understanding that, if and when business warranted, the lost salary would be paid in cash, or any indebtedness to the corporation cancelled to the extent of the lost salary. (R. 23a). In 1934 the corporation filed a petition for reorganization under old Section 77B of the Bankruptcy Act. (R. 25a). In 1936 Mr. Cummins died, owing the corporation $75,267.40. (R. 24a). A plan of reorganization of the corporation, under which the greater part of its indebtedness was converted into stock, was consummated in 1937. (R. 34a-46a). Meanwhile, the insolvent estate of Mr. Cummins was being administered in the Chancery Court for Davidson County, Tennessee. (R. 9a). The petitioner duly filed its sworn claim for the indebtedness of $75,267.40. (R. 25a).

In 1940, the reorganized corporation's business had improved to the extent that a cancellation of the indebtedness of Mr. Cummins would have been appropriate under the 1931 understanding, assuming that it survived his death and the bankruptcy proceeding (R. 27a); and both the District Court and the Court of

Appeals found that the indebtedness was extinguished in 1940 because of the return of good business conditions in that year. (R. 25a; 54a; App., *infra*, p. 8). But neither the representative of the estate of Mr. Cummins, nor any of the creditors who would have gained by the disallowance of petitioner's claim, interposed this defense in the Chancery Court proceeding, and on June 24, 1942, a decree was entered allowing petitioner's claim in full, as well as various other claims. (R. 9a). The Chancery Court proceeding was admittedly adversary in nature. (R. 53a). The petitioner received a small dividend on its claim and charged off the remainder as a bad debt. (R. 26a). This litigation ensued by reason of the contention of the Internal Revenue Service that petitioner was not entitled to the bad debt deduction.

The District Court held that, although the proceeding was adversary in nature, the Chancery Court decree allowing the claim was not binding on the Court. (R. 53a-54a). On appeal, the government sought to justify the decision on the sole ground that, because the defense which the District Court regarded as meritorious had not been actually considered and specifically adjudicated by the Chancery Court, the judgment was not entitled to full faith and credit. The Court of Appeals affirmed the judgment on the basis of the District Court's findings and conclusions and denied a petition for rehearing without opinion. (App., *infra*, pp. 8, 9).

REASONS FOR GRANTING THE WRIT

The question involved—the effect to be given in federal tax litigation to a state court decree involving property rights or contractual rights—is one which frequently arises and is of substantial importance.

The decision below is erroneous. In the first place, it fails to recognize and give effect to the principle of

Life Insurance Company v. Bangs, 103 U. S. 780, holding that a judgment is conclusive not only as to defenses actually asserted against a claim, but also as against defenses which might have been asserted but were not. (To the same effect, see *Jordan v. Johns*, 168 Tenn. 525). In the second place, it denies full faith and credit to the Chancery Court decree in contravention of Title 28, sec. 1738, U. S. Code, which extends to all courts, federal as well as state, the rule of Article IV, section 1, of the Constitution. See *Davis v. Davis*, 305 U. S. 32, 40; *Mills v. Duryee*, 7 Cr. 481, 485.

The decision below is in direct conflict with *Blair v. Commissioner of Internal Revenue*, 300 U. S. 5, in which this Court reversed a decision of the Seventh Circuit, 83 F. 2d 655, on another point. In *Blair*, this Court, referring to a state court decision, said (p. 10):

> ". . . To derogate from the authority of that conclusion and of the decree it commanded, so far as the question is one of state law, would be wholly unwarranted in the exercise of federal jurisdiction."

The decision below is also in direct conflict with an Eighth Circuit decision; *Helvering v. Rhodes' Estate*, 117 F. 2d 509, holding that a state court decree that a decedent did not own certain stock was binding and determinative, and with a prior Sixth Circuit decision, *Goodwin's Estate v. Commissioner of Internal Revenue*, 201 F. 2d 576, in which the Court held that it was bound by a consent decree entered in a state court proceeding, allowing claims against a decedent's estate, "where the consent of all beneficiaries adversely affected was given and accepted by the court as satisfactory evidence on the merits." (p. 582).[2] Both decisions correctly applied

[2] Certiorari was granted in *John Hancock Mutual Life Insurance Company v. Bartels*, 308 U. S. 180, and *Dickinson v. Petroleum Conversion Corp.*, 338 U. S. 507, because of an intracircuit conflict.

the *Blair* principle, which the present decision erroneously fails to apply.

CONCLUSION

For the foregoing reasons this petition for certiorari should be granted.

Respectfully submitted.

WILLIAM WALLER
American Trust Building
Nashville 3, Tennessee
Attorney for Petitioner

Of Counsel:

WALLER, DAVIS & LANSDEN
American Trust Building
Nashville 3, Tennessee

The *Blair* principle is also embodied in the Treasury Regulations cited by the Court in *Goodman's Estate*.

APPENDIX

No. 14,522

United States Court of Appeals

For the Sixth Circuit

TENNESSEE PRODUCTS & CHEMICAL CORPORATION, *Plaintiff-Appellant,* vs. UNITED STATES OF AMERICA, *Defendant-Appellee.*	ON APPEAL from the Judgment of the United States District Court for the Middle District of Tennessee.

Decided January 4, 1962

Before: MILLER, Chief Judge, SIMONS and CECIL, Circuit Judges.

PER CURIAM. Tennessee Products & Chemical Corporation, plaintiff-appellant, brought an action against United States, in the District Court for the Middle District of Tennessee, to recover approximately $29,000 for an over-payment of income taxes alleged to have been erroneously and illegally collected from the appellant.

The appellant corporation claimed that its former president, W. J. Cummins, was indebted to it in the amount of about $71,000, growing out of a 1931 agreement or action of the corporation reducing the salary of Mr. Cummins. It is the position of the appellant that this debt became worthless and uncollectible either in the

tax year 1942 or in the tax year 1946, and that the corporation was entitled to deduct the amount of the debt from its taxable income for one of those years.

Timely claims for refund were made for each of the tax years in question and upon the government's rejection of the claims, a complaint was filed in the District Court.

The issues were tried to the court and a judgment granted in favor of the United States, defendant-appellee. The trial judge found that there was a condition subsequent as a part of the arrangement for reducing the salary of Mr. Cummins, which became operative in 1940 and extinguished the debt. The substance of this condition was that when business warranted, the lost salary would be paid in cash, or if a debt had resulted by reason of the reduction, it would be cancelled.

The material facts are not in dispute and are set forth in detail in the trial judge's findings of fact, reported at . . . Fed. Supp. . . . . His conclusions of law and memorandum opinion are also reported with the findings of fact.

This appeal is from the order of the District Court dismissing the appellant's causes of action.

Upon consideration of the record of proceedings before the District Court, the briefs of the parties and oral arguments of counsel, we are of the opinion that the facts, as found by the trial judge, and the inferences drawn therefrom are correct and not clearly erroneous. The legal conclusions are sound and in accordance with applicable principles of law.

We conclude that judgment for the appellee was warranted upon the findings and conclusions of the trial judge and that the judgment of the District Court should be and it is hereby affirmed.

JUDGMENT

January 4, 1962

APPEAL from the United States District Court for the Middle District of Tennessee.

THIS CAUSE came on to be heard on the transcript of the record from the United States District Court for the Middle District of Tennessee, and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be and the same is hereby affirmed.

Approved for entry:

s/ LESTER L. CECIL
United States Circuit Judge

ORDER

February 13, 1962

It is hereby ordered that the last paragraph of the per curiam opinion in this case, dated January 4, 1962, be amended to read as follows: "We conclude that judgment for the appellee was warranted upon the findings of fact, conclusions of law and memorandum opinion of the trial judge, and that the judgment of the District Court should be and it is hereby affirmed."

It is further ordered that the petition for rehearing herein be and the same is hereby denied.

s/ LESTER L. CECIL
Circuit Judge